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FILED
AUG 7 1963
JOHN F. DAVIS, CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1963

No. 277

PANHANDLE EASTERN PIPE LINE COMPANY, *Petitioner*

v.

FEDERAL POWER COMMISSION, *Respondent*

On Petition For Writ of Certiorari to the United States Court of Appeals For the District of Columbia Circuit

BRIEF FOR INDEPENDENT NATURAL GAS ASSOCIATION OF AMERICA, AMICUS CURIAE, IN SUPPORT OF PETITION

JOHN T. MILLER JR.
1001 Connecticut Avenue, N.W.
Washington 36, D. C.
Counsel for Independent
Natural Gas Association
of America, *amicus curiae*

August 7, 1963.

Press of Byron S. Adams, Washington, D. C.

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BRIEF FOR INDEPENDENT NATURAL GAS ASSOCIATION OF AMERICA, AMICUS CURIAE, IN SUPPORT OF PETITION

This brief, *amicus curiae*, is filed with the consent of the parties.

INTEREST OF AMICUS CURIAE

Independent Natural Gas Association of America (INGAA) is a trade association which includes among its members most of the major pipeline companies engaged in the transportation and sale of natural gas

in interstate commerce subject to the jurisdiction of the Federal Power Commission (Commission) under the Natural Gas Act. For many years INGAA has appeared in rule-making, rate and certificate proceedings before the Commission involving issues affecting the general interests of the natural gas industry and participated before this Court and the various courts of appeals in cases arising out of Commission orders. In the instant case, INGAA has participated as *amicus curiae* at each stage of the proceedings in the court below.

The substantive question here presented concerns the proper return to be allowed on jurisdictional facilities financed by deferred income taxes accumulated by natural gas pipeline companies as a result of their use of Section 167 (liberalized depreciation) and 168 (accelerated amortization) of the Internal Revenue Code. Almost all of INGAA's pipeline company members have used one or both of these sections to defer payment of a portion of their federal income taxes. In the decision below, the Court of Appeals has approved the Commission's action of including the deferred tax accruals in the statement of Panhandle's capital and attributing to such sums a return of 1.5 percent. This has the practical effect of permitting Panhandle to earn only 1.5 percent on a portion of its rate base. If allowed to stand, this decision will result in substantial losses of revenue to the pipeline members of INGAA which, together with their affiliates, account for over 90 percent of the $320,000,000 of deferred taxes accumulated to the end of 1962 by the natural gas pipeline companies regulated by the Commission. Thus, *amicus* plainly has an immediate and significant interest in the issues presented.

REASONS FOR GRANTING THE WRIT

To minimize repetition, INGAA adopts Panhandle's petition which, it believes, fully demonstrates the need for review of the decision below by this Court. INGAA wishes only to supplement and amplify this showing by highlighting the following considerations.

I

This Case Will Affect Important Interests of the Natural Gas Industry and Must Be Speedily Resolved to Avoid Unjustified Injuries To Regulated Companies and a Multiplicity of Suits.

The question of the proper rate treatment by the Commission of deferred income tax accruals generated by the use of Sections 167 and 168 of the Internal Revenue Code requires a definitive resolution by this Court. There can be no doubt that the question is of general importance. This has already been recognized explicitly by the Commission in its petition for rehearing *en banc* and implicitly by the court below by its grant of rehearing *en banc*.

The *en banc* decision below, which in our view is plainly erroneous, was rendered by a sharply divided court, with a vigorous dissent joined in by four judges. This decision set aside the contrary ruling by the original panel. It represents a reversal of a position long held both by the Commission and the court below. As shown by the cases cited in Panhandle's petition (at pp. 5-6), for over seven years prior to its opinion issued in *Northern Natural Gas Co.* on March 7, 1961 (25 F.P.C. 431), on which its ruling herein is based, the Commission consistently held that Congress intended the full benefits of Sections 167 and 168 for the taxpayer pipeline companies. Similarly, a number of years ago the court below in *City of Detroit* v. *Federal*

Power Commission, 230 F. 2d 810 (D.C. Cir. 1955) *cert.* denied, 352 U.S. 829 (1956), had ruled with regard to Section 168 there involved (230 F. 2d at 822):

> "Though thus earmarked [in the reserve account], the funds are available for income-producing purposes. Unless this is permitted, it is difficult to see how Panhandle could benefit substantially from section [168]. This statute, unlike the Natural Gas Act itself, is not for consumer benefit. It has a different public policy and should be given effect as intended by Congress." * * *"

It was against the background of these earlier holdings that the natural gas pipeline companies elected to use Sections 167 and 168 and invested millions of dollars of deferred income tax[1] accruals in new plant facilities, as intended by Congress. However, in its decision in *Northern Natural* the Commission departed from its prior orders and practices and ruled for the first time—in the teeth of explicit recognition of its inconsistency with *City of Detroit* (see 25 F.P.C. at 437)—that natural gas pipeline companies must pass on the bulk of the benefits of Sections 167 and 168 to their customers.

The decision to invest deferred tax funds is entirely up to the taxpayer company, and the sums of money involved are substantial. The use of Section 167 by natural gas pipeline companies generated $40,000,000 of deferred income taxes in 1962 alone.

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[1] Section 168 has not been available since 1957. As a consequence the accumulated deferred income taxes attributable to this source are now declining each year. However, at the end of 1961 natural gas pipeline companies still had more than $70,000,000 of deferred income taxes arising from use of Section 168 which had been available for corporate purposes prior to the time when the Commission changed its position. See Federal Power Commission, Statistics of Natural Gas Companies, 1961, Table 14.

The affirmance by the court below of this change by the Commission in its position will, if not reversed, not only reduce the earnings which the natural gas pipeline industry expected on the basis of the pre-1961 decisions of the Commission and of the court below to be permitted to earn on jurisdictional facilities financed in the past by deferred tax accruals, but also deter pipeline companies from investing additional large amounts of deferred taxes in new jurisdictional plant. An authoritative ruling by this Court is required to remove uncertainty, and to enable the companies to make informed decisions with regard to the investment of additional deferred tax funds.

Finally, review by this Court is needed to put this problem to rest in the cases pending in other circuits. See *Southern Natural Gas Co.* v. *Federal Power Commission*, Third Circuit Case No. 14399,[2] arising out of Opinion No. 379, issued February 18, 1963, and *El Paso Natural Gas Co.* v. *Federal Power Commission*, Fifth Circuit Case No. 20180, arising from Opinion No. 366, issued October 19, 1962. These cases involve the question here presented inasmuch as the Commission included accumulated deferred taxes in the capitalization of each company and attributed to the deferred taxes a "cost" of 1.5 percent. El Paso specifically argues that its deferred taxes are not invested in jurisdictional plant.

[2] This case is being held in abeyance pending final determination of the instant case.

II

The Commission and Court Below Have Plainly Acted Contrary to the Intent of Congress In Enacting Sections 167 and 168 of the Internal Revenue Code.

It is clear that Congress intended these Sections as a stimulus to business investment as a matter of national policy. The Committee reports and the House debates are replete with expressions of this purpose. To limit examination, for brevity, to liberalized depreciation, the Reports of the House and Senate committees considering Section 167 state:

> "More liberal depreciation allowances are anticipated to have far-reaching economic effects. The incentives resulting from the changes are well timed to help maintain the present high level of investment in plant and equipment. The acceleration in the speed of the tax-free recovery of cost is of critical importance in the decision of management to incur risk. The faster tax writeoff would increase available working capital and materially aid growing businesses in the financing of their expansion. For all segments of the American economy, liberalized depreciation policies should assist modernization and expansion of industrial capacity, with resulting economic growth, increased production, and a higher standard of living."[3]

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[3] Report of the Committee on Ways and Means, House of Representatives, to accompany H.R. 8300, a bill to revise the internal revenue laws, H. Rep. No. 1337, 83rd Cong., 2d Sess., p. 24 (1954); Report of the Committee on Finance, United States Senate, S. Rep. No. 1622, 83rd Cong., 2d Sess., p. 26 (1954). See also, the annual address of the President to Congress, 100 Cong. Rec. 571, January 21, 1954; Statement of the Under Secretary of the Treasury at Hearings before the Senate Committee on Finance, 83rd Cong., 2d Sess. 104 (1954).

It is equally clear from both the terms of the statutory provisions and from their legislative histories, that the deferred tax legislation was intended to and does apply equally to all types of new tangible depreciable assets, and to be available to all taxpayers.[4] Congress has repeatedly been advised of the use of these deferred tax provisions by natural gas pipelines and other regulated companies and of the Commission's determination that these tax provisions were for the benefit of the taxpaying pipeline company.[5] While it also has been urged to amend the statute to eliminate this result, Congress has not done so.[6] Even though it has amended both Section 167 and Section 168, it has not changed the law in any way to indicate that either the Court's decision or the Commission's opinions, orders and rulings *prior* to the *Northern Natural* case in 1961 had misinterpreted the Congressional intent.

Thus, Congress clearly intended to provide funds and incentives to stimulate investment by regulated industries in jurisdictional plant. By reversing its position and, in practical effect, imposing a 1.5 percent return limitation on jurisdictional plant financed by deferred taxes, the Commission has undertaken to do

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[4] See, for example, H. Rep. No. 1337, 83rd Cong., 2d Sess., pp. 23, 24 (1954); S. Rep. No. 1622, p. 25 (1954); 100 Cong. Rec. 8997, 8998, June 28, 1954.

[5] See *Amere Gas Utilities Co.*, 15 F.P.C. 781, 782 (1956); *El Paso Natural Gas Co.*, 22 F.P.C. 260, 266-267 (1959); Annual Report of the Federal Power Commission to Congress for 1956 (pp. 75-76), and for 1957 (p. 75). See also Rapid Amortization in Regulated Industries, S. Rep. No. 1380, 85th Cong., 2d Sess., 81 (1958).

[6] See Technical Amendments Act of 1958, Title I, §§ 9, 89(b), 72 Stat. 1608, 1665 and Pub. L. 85-165, § 4, 71 Stat. 414 (1957).

what Congress declined to do. It has ruled in effect that the deferred tax legislation intended to place the taxpayer who invests deferred tax accruals in interstate natural gas pipeline facilities in an inferior category. This ruling, which takes away a substantial part of the benefits granted by the tax legislation, directly contradicts the Congressional purpose of stimulating investment in *all* productive facilities.

By contrast, the allowance of a full return on plant financed by deferred tax accruals, properly sought here by Panhandle, permits Sections 167 and 168 to stimulate effectively investment in new jurisdictional plant. Unlike the Natural Gas Act itself, Sections 167 and 168 are not for consumer benefit. They have a different public policy and should be given effect as intended by Congress.[7] However, it is important to note that the Commission can carry out this intent of Congress by permitting Panhandle to earn a full return without, at the same time, penalizing the gas consumers.[8]

Finally, the Commission's limitation of the rate of return on plant financed by deferred taxes is not only inconsistent with the Congressional intent to stimulate investment in all productive facilities, but it also vir-

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[7] *City of Detroit* v. *Federal Power Commission*, 230 F. 2d 810, 822 (1955), *cert.* denied, 352 U.S. 829 (1956). See also, *El Paso Natural Gas Co.*, 22 F.P.C. 260, 266 (1955), *aff'd.* as to this issue, 281 F. 2d 567 (5th Cir. 1960), *cert.* denied *sub nom.*, *California* v. *Federal Power Commission*, 366 U.S. 912 (1961); *Phillips Petroleum Co.*, 24 F.P.C. 537, 570 (1960), *aff'd sub nom. State of Wisconsin* v. *Federal Power Commission*, 303 F. 2d 380 (D.C. Cir. 1961), *aff'd.* 373 U.S. 294 (1963), and S. Rep. No. 1380, 85th Cong., 2d Sess. 4, 67-68 (1958).

[8] See Petition for Writ of Certiorari, p. 16.

tually negates the intention of Congress to recoup the current tax revenue loss to the government caused by the deferral of taxes. This is clear, since Section 167 was designed to "broaden the tax base"[9] by financing new plant which would produce additional taxable income. The report of the Committee on Ways and Means of the House of Representatives states, in this regard:

> "If there were no stimulus to investment and all eligible taxpayers adopted the new formula, the loss in the fiscal year 1955 would be about $375 million. In the second and immediately subsequent years there would be greater losses if the effect on investment were ignored but it is highly likely that by that time the stimulus which the new formula brings will have produced a volume of additional investment and taxable income which will result in there being no net revenue loss under this provision."[10]

But if the Commission is allowed to limit the rate of return on jurisdictional plant financed by the deferred tax accruals of the natural gas pipeline companies to only 1.5 percent, it will frustrate this purpose of Congress by reducing pipeline taxable earnings, thus denying the Treasury substantial corporate tax revenues which would serve to offset current tax revenue losses arising from use of liberalized depreciation.

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[9] Statement by Congressman Reed, Chairman of the House Ways and Means Committee, during debates on the proposed legislation. 100 Cong. Rec. 3421, March 17, 1954.

[10] H. Rep. No. 1337, 83rd Cong., 2d Sess., p. 25.

III

A Return of 1.5 Percent Will Deter Investment of Deferred Taxes In New Pipeline Plant, Contrary to the Internal Revenue Code.

The court below and the Commission both failed to recognize that the Congressional intent in Sections 167 and 168 embraced a dual incentive. It would not effectuate the Congressional purpose if taxpayers were to use Sections 167 and 168 merely as a device for deferring the payment of income taxes. Congress also intended that the funds generated by the use of these Sections should be used for investment in new plant facilities. When this second incentive is recognized, it becomes apparent that the holding below falls far short of effectuating the Congressional intent.

There is no evidence of record in this case to support a finding that 1.5 percent is sufficient to attract the investment of deferred tax accruals in jurisdictional natural gas pipeline facilities. Quite the contrary, Panhandle "made clear to the Commission that it would not feel justified in making the elections without official assurance of full benefit therefrom."[11] It would be pure fiction, we submit, to assume that a return of 1.5 percent would have provided sufficient incentive to attract the investment of the millions of dollars of deferred tax accruals in jurisdictional facilities prior to 1961 when that limitation on return was first imposed by the Commission. Until that time the industry had every reason to believe that the pipeline companies would be allowed a far better return on such investments.[12]

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[11] Quotation from the dissent in the court below. See Appendix A to Petition for Writ of Certiorari, pp. 45a-46a.

[12] See discussion at pages 3-4 above.

It is clear that natural gas pipeline companies are not compelled, either by the Internal Revenue Code or the Natural Gas Act, to invest in jurisdictional facilities. Thus, under the Internal Revenue Code, Congress left to each taxpayer the decision how to use deferred tax accruals, and the Natural Gas Act explicitly leaves pipeline expansion to the initiative of the pipeline companies.[13] Section 7(a) specifically provides that the "Commission shall have no authority to compel enlargement of transportation facilities".[14]

The deferred tax accruals are the pipeline company's funds, subject to later payment of the deferred tax liability. As it invests such funds at its own risk,[15] the company has a duty to its stockholders to weigh the alternative investment opportunities prudently, to balance investment in new jurisdictional facilities against other income producing possibilities. Consequently, since such investment cannot be compelled, deferred tax accruals must be attracted to investment in new interstate natural gas pipeline facilities. To assure this result, a return "commensurate with returns on investments in other enterprises having corresponding risks" must be allowed on facilities financed with such funds. *Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U.S. 591, 603 (1944). A return of 1.5 percent has not been shown to and indeed does not meet this standard.

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[13] See *Central West Utility Co.* v. *Federal Power Commission*, 247 F. 2d 306 (3d Cir. 1957); *Panhandle Eastern Pipe Line Co.* v. *Federal Power Commission*, 204 F. 2d 675 (3d Cir. 1953).

[14] 52 Stat. 824 (1938), 15 U.S.C. § 717f(a).

[15] These are facts which the Commission itself recognizes. See Brief for the Commission in the court below, p. 10.

IV

The Commission May Not Lawfully Ordain An Identical Rate of Return For Very Different Pipeline Companies.

Even if it be assumed *arguendo* that the Commission could properly allow less than a full return on jurisdictional plant financed by deferred tax accruals, the affirmance of the Commission's order by the court below would nevertheless be erroneous. The Commission applied to Panhandle the same 1.5 percent return on deferred tax accruals that it applied to Northern Natural Gas Company (25 F.P.C. 431 (1961)) and Kansas-Nebraska Natural Gas Company (25 F.P.C. 448 (1961)) on the ground that the "principles applied in the *Northern* case are equally applicable to Panhandle in the present case" (25 F.P.C. at 550).

There is no indication that, in arriving at this conclusion, the Commission examined all relevant facts and circumstances of each of these three quite different companies. Certainly there is no evidence in the record of the *Panhandle* case to support such a comparison.

In these circumstances, the Commission's action is patently in error. The factors involved in a proper determination of the rate of return allowed for a particular natural gas pipeline company are varied and complex. Each case stands independently of all others and is to be decided on the record made in that case. It is well established that rate of return cannot be determined by *a priori* judgment. "A rate of return may be reasonable at one time and become too high or too low by changes affecting opportunities for investment, the money market and business conditions generally. * * * [N]o proper rate can be established for all

cases." *Bluefield Water Works & Improvement Co.* v. *Public Service Commission*, 262 U.S. 679, 693 (1923).

The Natural Gas Act contains only the conventional standards of rate-making. There is nothing novel in its provisions. *Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U.S. 591, 616 (1944). Under such standards, the Commission may not lawfully preordain the return to be allowed natural gas pipeline companies, as it has attempted to do here. Such a procedure forecloses the Commission from the exercise of that fair and enlightened judgment, having regard for all relevant facts, which it must employ in each rate proceeding under the Natural Gas Act.

CONCLUSION

We respectfully submit that this Court should review this decision of the Court of Appeals. It sanctions a drastic departure from the Congressional purpose in enacting the liberalized depreciation and accelerated amortization provisions of the Internal Revenue Code, and the regulatory provisions of the Natural Gas Act. The issue involved is of substantial importance to the entire natural gas industry.

The petition for writ of certiorari should be granted.

Respectfully submitted,

JOHN T. MILLER JR.
1001 Connecticut Ave., N.W.
Washington 36, D. C.

August 7, 1963

CERTIFICATE OF SERVICE

I, John T. Miller Jr., attorney for Independent Natural Gas Association of America and a member of the Bar of the Supreme Court of the United States, do hereby certify that I have served upon the following named attorneys a copy of the foregoing brief *amicus curiae* in support of petition for writ of certiorari to the United States Court of Appeals for the District of Columbia Circuit by depositing true and correct copies thereof in the United States Mail, first class postage prepaid, on August 7, 1963, addressed as follows:

Honorable Archibald Cox
Solicitor General
Department of Justice
Washington, D. C. 20530

Richard A. Solomon
General Counsel
Federal Power Commission
Washington 25, D. C.

Howard E. Wahrenbrock
Solicitor
Federal Power Commission
Washington 25, D. C.
Counsel for Respondent

Harry S. Littman
317 Wyatt Building
Washington 5, D. C.
Counsel for Petitioner

JOHN T. MILLER JR.
Attorney for Independent
Natural Gas Association
of America, *amicus curiae*

August 7, 1963
Washington, D. C.